FISCAL NOTE
HB 38 - SB 48
FIRST EXTRAORDINARY SESSION

April 16, 1999

SUMMARY OF BILL:

1. Extends the franchise and excise tax to limited liability companies and limited liability partnerships.
2. Amends the definition of "business earnings" to exclude a taxpayer engaged exclusively in the buying, selling, or holding of securities on its own behalf and not as a broker, and its gain or losses from the sale or exchange of such securities are treated as gains or losses from the sale or exchange of capital assets.
3. Repeals the professional privilege tax.
4. Repeals the Hall income tax.
5. Exempts from sales and use tax, *food and food products for off-premises consumption*. Food or food products is defined as items that are eligible to be purchased with food stamps.
6. Reduces the sales tax from 6% to 5% on the following items: 1) Tangible personal property sold at retail; 2) Lease or rental of property; 3) Services, and 4) Interstate telecommunication services.
7. Imposes a 2% income tax on the federal adjusted gross income of every individual.
8. Authorizes a standard personal exemption of $4,000 per individual. Every individual, except a claimed dependent, filing a state income tax return would be allowed one exemption. Taxpayers filing jointly would be allowed two exemptions. A taxpayer would be allowed a personal exemption for each claimed dependent. The bill would require a couple to file their state income tax return in the same manner, individually or jointly, as they file their federal income tax return.
9. Any interest income earned on obligations of the United States or its possessions would be excluded from state income tax, if the income is excluded from federal income tax.
10. Provides a taxpayer credit for income taxes accrued to another state; however, the credit could not include any accrued interest or penalties owed another state because of back taxes and the tax credit derived from income tax accrued to another state would not be allowed to exceed the income tax due in Tennessee. The credit for taxes owed to another state must be taken in the year in which they are accrued. A non-resident individual would be liable for the payment of this tax for any income such individual has received from sources within this state.
11. Mandates that employers withhold 2% of an employee's wages paid at the same time and in the same manner as amounts are withheld for federal tax purposes.
12. Requires any employer required to withhold wages to register with the Department of Revenue by July 1, 1999. Any employer who fails to register by October 1, 1999, would be subject to a penalty of up to $1,000. Any employer who would become subject to these provisions after September 1, 1999, would have 30 days to register in order to avoid the penalty.
13. Requires state income tax returns to be filed by April 15 of each year.
14. Provides that revenues generated under this bill would be earmarked for the General Fund.
15. Contains a schedule establishing allocation of revenues generated from the state income tax. A summary of the allocation is as follows:
    - July 1, 1999 - $150,227,916 - This is an aggregate amount. The bill specifies the amount individual cities and counties would receive.
    - July 1, 2000 - $156,987,872 - This is an increase of 4.5% over FY00 and is an aggregate amount. The bill specifies the amount individual cities and counties would receive.
    - July 1, 2001 - The distribution would be adjusted by an amount equal to the percentage change in the state income tax.
    - The above allocations would be distributed in 12 equal monthly installments.

- Allocations for Premier Type Resort Areas are as follows:
  - July 1, 1999
    - Gatlinburg $133,700
    - Sevierville $246,000
  - July 1, 2000
    - Gatlinburg $139,717 [an increase of 4.5% over the 1999 amount]
    - Sevierville $257,070 [an increase of 4.5% over the 1999 amount]
  - July 1, 2001
    - The distribution would be adjusted by an amount equal to the percentage change in the state income tax collections from the preceding fiscal year to the next fiscal year.
  - Allocations for these areas would be distributed in 12 equal monthly payments.
- Allocations to the General Fund for K-12 Education Purposes
  - July 1, 1999 - $33,208,200
  - July 1, 2000 - $34,702,569 [an increase of 4.5% over the 1999 amount]
  - July 1, 2001 and thereafter - The distribution would be adjusted by an amount equal to the percentage change in the state income tax collections from the preceding fiscal year to the next fiscal year.
  - The allocation would be distributed in 12 equal monthly payments.
- Allocations specifically earmarked for Education Purposes:
  - July 1, 1999 - $237,546,800
  - July 1, 2000 - $248,236,406 [an increase of 4.5% over the 1999 amount]
  - July 1, 2001 and thereafter - The distribution would be adjusted by an amount equal to the percentage change in the state income tax collections from the preceding fiscal year to the next fiscal year.
  - The allocation would be made in 12 monthly installments.
- Allocations for Incorporated Municipalities
  - The allocations for the several incorporated municipalities would be distributed based on the sales and use tax distribution method established under present law.
  - The allocation would be in 12 equal monthly payments.
  - Before distribution, a deduction of 1% of the monthly allocation would be apportioned and transmitted to the University of Tennessee.
  - July 1, 1999 - $16,758,600
  - July 1, 2000 - $17,512,737 [an increase of 4.5% over the 1999 amount]
  - July 1, 2001 and thereafter - The distribution would be adjusted by an amount equal to the percentage change in the state income tax collections from the preceding fiscal year to the next fiscal year.
- Allocations to the State Sinking Fund
  - July 1, 1999 - $3,351,700
  - July 1, 2000 - $3,502,527 [an increase of 4.5% over the 1999 amount]
  - July 1, 2001 and thereafter - The distribution would be adjusted by an amount equal to the percentage change in the state income tax collections from the preceding fiscal year to the next fiscal year.
  - The allocation would be made in 12 equal monthly payments.
- Allocations for Administrative Fee
  - An amount equal to 0.000872% of the tax collected would be distributed to the Department of Revenue as an administrative fee.
- Additional Amounts for Municipalities and Counties
  - All remaining amounts of the tax revenue would next be distributed so that in the 1999-2000 fiscal year and thereafter each municipality and county would receive, in addition to the revenues allocated under present law sales and use tax provisions, an additional sum equal to the amount which would have been received pursuant to such provisions if the tax rate had not been reduced by this bill.

16. Provides that for the purposes of promulgating regulations, this bill would take effect upon becoming law; for the purposes of employer registration, the bill would take effect July 1, 1999, and for all other purposes, the bill would take effect January 1, 2000.

ESTIMATED FISCAL IMPACT:

Increase State Revenues - Net Impact $297,858,736 FY00
Net Impact $591,342,472 FY01

Increase State Expenditures - Dept. of Revenue
Exceeds $3,000,000 Recurring
Exceeds $2,000,000 One-Time

Decrease Local Govt. Revenues - Net Impact $207,802,159 FY00
Net Impact $418,229,318 FY01

Estimate assumes the following:

- Extension of the franchise and excise tax to LLC's and LLP's would increase state revenues approximately $75,000,000 in FY00 and $150,000,000 in FY01.
- Repealing the professional privilege tax is estimated to decrease state revenues approximately $10,950,000 in FY00 and $21,900,000 in FY01.
- Eliminating the Hall income tax would result in an estimated decrease in revenue of approximately $88,500,000 in FY00; of which, $55,312,500 is the state portion and $33,187,500 is the local government portion. The estimated decrease in revenues in FY01 is $184,000,000; of which, $115,000,000 is the state portion and $69,000,000 is the local government portion.
- Hall income tax is apportioned 5/8ths to the state and 3/8ths to local government.
- Removing the sales tax on Food is estimated to decrease state revenues approximately $204,330,000 in FY00 and $408,660,000 in FY01 and is estimated to decrease local government revenues approximately $76,623,750 in FY00 and $153,247,500 in FY01.
- Decreasing the sales tax on certain other items by 1% is estimated to decrease state revenues approximately $261,309,091 in FY00 and $522,618,182 in FY01 and is estimated to decrease local government revenues approximately $97,990,909 in FY00 and $195,981,818 in FY01.
- Based on information provided by the Department of Revenue, the Comptroller's Office and 1996 federal data, taxable income of Tennessee residents would generate approximately $1,509,520,653.
- The increase in state expenditures is estimated to exceed $5,000,000 for implementation of a new tax structure.
- The impact for FY00 represents six months of tax collections.

Apportionment Note: The bill outlines apportionment of the increase in state revenues in a highly detailed format to both state and local governments.

CERTIFICATION:

This is to duly certify that the information contained herein is true and correct to the best of my knowledge.

James A. Davenport

James A. Davenport, Executive Director